No. 89-475

IN THE

Supreme Court of the United States

OCTOBER TERM, 1989

PEAT MARWICK MAIN & CO.,

Petitioner,

—v.—

PHILIP D. ROBERTS, et al.,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

REPLY BRIEF IN FURTHER SUPPORT OF PETITION

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Reference is made to Peat Marwick's statement pursuant to Rule 28.1 at page ii of the Petition for a Writ of Certiorari ("Pet.").

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This reply brief responds to the principal new arguments advanced by respondents in the brief in opposition ("Br. Op.").

The Ninth Circuit's Treatment of Section 10(b) Aiding and Abetting Liability Premised on Silence or Inaction Conflicts With Decisions of Other Circuit Courts and Principles Announced By This Court in *Dirks* v. *SEC* and *Chiarella* v. *United States*.

(1) Respondents assert that "There Is No Conflict Among The Courts Of Appeals As To The Pleading Issue Raised By This Appeal" (Br. Op. 13). But respondents can support that proposition only by redefining, in a fashion flatly at variance with the Ninth Circuit, the matter at issue here: aiding and abetting claims premised on a defendant's silence or inaction.

(a) Respondents' central thrust is *not* that conflict is lacking among the circuits on the issue of aiding and abetting liability premised on silence or inaction. (Indeed, the brief in opposition at one point concedes that with respect to "silence or inaction" there *is* a "discernible distinction among the circuit courts insofar as application of aiding and abetting principles are concerned" (Br. Op. 14, n.11).)

Rather, their principal argument is that this case does not involve a claim premised on silence or inaction at all (Br. Op. 4, 7-8, 14, 16). (*E.g.*, "This case is not about silence or inaction or, stated another way, 'whistleblower' liability" (Br. Op. 14).) Yet that is precisely the issue which the Ninth Circuit understood the complaint to raise and which its opinion addressed. ("Defendants may be liable for aiding and abetting *based on their silence* if they have a duty to disclose knowledge that would be material to investors." 857 F.2d at 652-53 (Pet. 14a) (emphasis added).) Thus, even while reading the Fourth Amended Complaint far more expansively than did the district court, *compare* 670 F. Supp. at 1482 (Pet. 41a-42a) *with* 857 F.2d at 652 (Pet. 13a), the court of appeals recognized that it was silence or inaction, not affirmative conduct, as respondents would now have it, that was at issue.[1]

Nor can the fact that in this case potential liability is premised on silence be avoided by reference to the reports on financial statements and tax returns that Peat Marwick did eventually prepare (Br. Op. 4-5 & n.4, 14). Both the district court and the

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1 The court of appeals adopted its characterization of the claim as one predicated on "silence" *after* setting forth its gloss on the allegations of the complaint cited at page 7 of the Petition (and at page 3 of the Br. Op.). As this fact itself suggests, the allegations of the complaint as to "participation" in the preparation and "effective control" of the offering memoranda and "investigation" in connection therewith simply reduce themselves to the core allegation that Peat Marwick permitted use of its name while allegedly knowing of a fraud. The court refers to no allegation that Peat Marwick actively participated in any fraud, or authored any false report, only that it permitted use of its name and hence its reputation without disclosing its alleged knowledge of fraud. 857 F.2d at 653 (Pet. 14a-15a). The court of appeals held that this silence was itself actionable.

Ninth Circuit held in the context of primary liability and based on respondents' own "acknowledge[ment]" as to the timing of the preparation and dissemination of these reports, 857 F.2d at 649 (Pet. 7a), that these allegations were legally irrelevant. 857 F.2d at 652 (Pet. 12a-13a); 670 F. Supp. at 1481 (Pet. 40a). The court noted those allegations in listing the facts in the complaint, 857 F.2d at 652 (Pet. 13a), but did not rely on them in explaining its reasons for sustaining the aiding and abetting claim. 857 F.2d at 652-53 (Pet. 14a-15a). They remain without legal effect. The claim at issue is, as the Ninth Circuit recognized, one premised on Peat Marwick's silence.

(b) Although respondents repeatedly promise to explain their somewhat muted contention that no conflict among the circuits exists even as to the standards to be applied on the issue of silence or inaction (*see, e.g.*, Br. Op. 13, 16), no such explanation is offered. The Petition for Certiorari cites cases from both the Second and Seventh Circuits in conflict with the decision of the Ninth Circuit on this issue. Respondents seek to portray the *Roberts* decision as simply part of a "well settled line of decisional authority" holding that aider and abettor liability may attach even absent an independent duty to disclose if the evidence shows the requisite scienter (Br. Op. 17). The decisions of the Second and Seventh Circuits simply cannot be reconciled with this approach, however.

Respondents offer the suggestion that the Second Circuit's decision in *IIT* v. *Cornfeld*, 619 F.2d 909 (2d Cir. 1980), holds that the presence of scienter avoids any need to find an independent duty in such cases (Br. Op. 16-17). The very language quoted by respondents makes clear, however, that only the existence of such independent duty or clear evidence of both scienter "*and* a conscious and specific motivation for not acting on the part of an entity with a direct involvement in the transaction" is required. 619 F.2d at 927 (emphasis added). Respondents do not account for these additional requirements, requirements plainly not met by the pleading here nor required by the Ninth Circuit decision as to which review is sought. Respondents offer even less by way of avoiding the differences between the Seventh Circuit approach and that followed here,

suggesting only a series of irrelevant factual distinctions which do not negate the fundamentally different nature of the Seventh and Ninth Circuits' legal analyses described in the Petition (Pet. 13-16).

(2) Respondents seek to avoid the conflict in approach between the Ninth Circuit's *Roberts* decision and this Court's rulings in *Dirks* v. *SEC*, 463 U.S. 646 (1983), and *Chiarella* v. *United States*, 445 U.S. 222 (1980), by reference to the fact that this Court's decisions in those cases concerned insider trading and involved primary as opposed to secondary liability (Br. Op. 19-20). But these factual distinctions hardly alter or make less instructive this Court's recognition in those decisions that only the existence of a duty to disclose can render non-disclosure actionable. Certainly the lower courts have read *Dirks* and *Chiarella* as providing direct guidance in cases asserting secondary liability outside the insider trading context. *See Schlifke* v. *Seafirst Corp.*, 866 F.2d 935, 947-48 (7th Cir. 1987); *Barker* v. *Henderson, Franklin, Starnes & Holt*, 797 F.2d 490, 495-96 (7th Cir. 1986); *Cairns* v. *Renneisen, Renneisen & Redfield*, [1987] Fed. Sec. L. Rep. (CCH) ¶ 93,626 at 97,839 (E.D. Pa. 1987).

Respondents also purport to distinguish the *Dirks* and *Chiarella* duty discussion on the bases set forth in *Deutschman* v. *Beneficial Corp.*, 841 F.2d 502 (3d Cir. 1988), *cert. denied*, 109 S.Ct. 3176 (1989), a decision they quote at length (Br. Op. 20-21). But *Deutschman*'s holding that *Dirks* and *Chiarella* were inapplicable was premised, as the last sentence of *Deutschman* quoted by respondents reflects, on a situation involving "affirmative misrepresentation", not a failure to disclose. The sentence immediately following, not quoted by respondents, makes the point even more plainly: "Except to the extent that other federal statutes may have imposed a disclosure obligation . . . , [defendant] and its officers *were free to keep quiet* about its business affairs so long as they stayed out of the market." *Deutschman* v. *Beneficial Corp.*, *supra*, 841 F.2d at 506 (emphasis added). The decision below in this case defines the circumstances in which that freedom "to keep quiet" may be abridged. The teachings of *Chiarella* and *Dirks* cannot be ignored in such context.

Whether A Private Right of Action For Aiding and Abetting A Violation of Section 10(b) Exists Is An Important Question Ripe for This Court's Review.

The Petition also raises an issue broader than that of the standards to be applied in an aiding and abetting claim premised on silence: whether an implied private right of action exists at all for aiding and abetting a violation of Section 10(b) or Rule 10b-5.

(a) Respondents suggest that, notwithstanding this Court's reservation of that question on two separate occasions, the question is not an important one requiring review (Br. Op. 10). We do not believe this Court bothers to reserve issues lacking in importance. The most comprehensive recent scholarly treatment of this subject, after analyzing the issue in terms of the tests this Court has applied, concludes that this Court's review of this "overarching question" is, at least absent explicit Congressional guidance, important to improve the proper application of the federal securities laws. Bromberg & Lowenfels, *Aiding and Abetting Securities Fraud: A Critical Examination*, 52 Albany L. Rev. 637, 773 (1988). The Petition presents an opportunity to decide this issue not by acquiescence in a series of lower court decisions originating before this Court developed its rigorous standards for implied rights of action,[2] but by affirmative consideration of the application of those standards to the statutory language and schema.

(b) Contrary to respondents' contention (Br. Op. 9), the broader point as to the existence of a private right of action was raised below and preserved for this Court's review. Since the district court had dismissed the complaint for failure to state a claim and the Ninth Circuit had previously recognized the existence of a private cause of action for aiding and abetting, there was no occasion to challenge this Ninth Circuit law until the court of appeals reversed the dismissal. Then, in its petition for

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2 The Ninth Circuit recognized a private right of action for aiding and abetting before this Court's decision in *Cort* v. *Ash*, 422 U.S. 66 (1975), established a framework for analysis.

rehearing, Peat Marwick explicitly referred to the fact that the "Supreme Court has expressly reserved judgment on whether 'civil liability for aiding and abetting is appropriate under [section 10(b) and Rule 10b-5]' ", citing this Court's decision in *Ernst & Ernst* v. *Hochfelder*, 425 U.S. 185 (1976), explicitly noting that this Court had recognized the question to be one of statutory construction and drawing the Ninth Circuit's attention to the leading critique of the recognition of such claim (Petition for Rehearing 6-7 n.6). Thus the question was raised and preserved. This question is, in any event, clearly a step on the path to determination of the elements of an aiding and abetting claim if any exists.

* * *

In this case the court of appeals held, as lower courts interpreting the decision have recognized, that a valid cause of action exists when the complaint alleged that "investors relied on Peat, Marwick's reputation when deciding to invest and that they would not have invested had Peat, Marwick disclosed the alleged fraud." 857 F.2d at 653 (Pet. 15a).[3] This flat acknowledgment of potential liability for a professional based not on any report or statement made by it, but on the use of the defendant's name and its failure to speak, when coupled with the Ninth Circuit's refusal to require, as other circuits have, that an independent duty to speak be present where a claim is asserted in such circumstances, represents an extension of existing law and poses a serious and important conflict among the Circuits. Such holding is also at variance with more general guidance from this Court in *Chiarella* and *Dirks*. The decision and the questions arising from it presented in the Petition warrant review.

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3 This is the interpretation of *Roberts* adopted in *In re Worlds of Wonder Securities Litigation*, [1989] Fed. Sec. L. Rep. (CCH) ¶ 94,449 at 92,888 (N.D. Cal. 1989) (to be officially reported at 721 F.Supp. 1140).

CONCLUSION

For the foregoing reasons and the reasons set forth in the Petition, Peat Marwick's petition for a writ of certiorari should be granted.

Dated: New York, New York
November 22, 1989

Respectfully submitted,

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